IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO **DIVISION OF FINANCIAL MANAGEMENT** **AUGUST 2004 VOLUME XXVII NO. 2**

THe Division of Financial Management (DFM) forecast is produced twice a year and the August projection sets the tone until the legislative session begins in January. In this spirit, we have included our current FY 2005 General Fund revenue forecast on the back page of this report. This revision is the second official projection of FY 2005 General Fund collections, and the first to include impacts from law changes made during the 2004 Idaho legislative session. It also includes updated factors from the July 2004 *Idaho Economic Forecast*. These factors play a key role in determining the revenue forecast, so an understanding of these factors is vital to understanding the revenue forecast. To this end, this *Outlook* provides a synopsis of both the Idaho and U.S. economic forecasts that were used to prepare the current FY 2005 General Fund revenue forecast.

This should be the state's strongest year in recent memory. After stalling in 2002, the nonfarm employment advanced just under 1% in both FY 2003 and FY 2004. It is projected to advance 1.8% during the current fiscal year. Idaho personal income should rise 5.4% in FY 2005. An important component of Idaho personal income is wages and salary payments. Not only is it the largest component of personal income, but it also drives the Individual Income Tax and Sales Tax forecasts. Interestingly, it is expected to improve slightly faster than total income. Specifically, Idaho wages and salary payments growth accelerates from 2.6% in FY 2003 to 5.4% in FY 2005.

Incidentally, DFM is not the only one bullish about Idaho's prospects. Global Insight, one of the nation's premier economic forecasting firms, recently ranked Idaho near the top in several categories. Specifically, Idaho is expected to experience the 10th fastest nonfarm job growth in the nation from 2004 to 2006. It should have the 23rd fastest personal income growth over this same period.

One of the reasons Idaho's economy should do well is because it started its recovery before many states. For example, while the nation was still in the throes of the jobless recovery, Idaho actually added jobs. By 2003 the Gem State had gained back all of the jobs it lost during the recession. Not all states have been this fortunate. None of the West Coast states are expected to top their pre-recession employment peaks until 2005. Some eastern states, including New York, are not expected to recover their jobs losses until 2006 at the earliest. One of Idaho's brightest sectors is high-tech. Global Insight noted that from 1995 to 2003 Idaho's high-tech rank, based on its percent of the state's total employment, had climbed from 17th to 8th in the nation. Boise's ranking among metro areas rose from 31st in 1995 to 12th in 2003. Thus, Idaho is well positioned to take advantage of what is considered one of the economy's hottest growth sectors.

Driving the improved outlook for Idaho is the return of more prosperous times at the national level. A key assumption of the U.S. forecast is the economy successfully transitions from policy-supported growth to self-sustaining growth. Accommodative monetary and fiscal policies have kept the recovery moving over the last few years despite the lackluster job market. However, the stimulative effects of tax cuts and low interest rates are quickly coming to an end. The rising federal deficit will put Congress in a less generous mood and the Federal Reserve has already raised its short-term interest rate target twice.

During the next few months the national economy will be tested to see if it can stand on its own legs. In order for the economy to pass this test, it must create a steady stream of jobs. These jobs, in turn, will generate income that will fuel further economic growth. According to Global Insight's June 2004 macroeconomic forecast, U.S. nonfarm employment should expand nearly 2% during FY 2005. Not only is this the strongest showing since FY 2000, but it is also the strongest year of the forecast. Admittedly, the disappointing July 2004 employment numbers have cast some doubt on this forecast. The U.S. Department of Labor reported only 32,000 jobs were added in July 2004, which was well below economists' expectations. However, employment gains in other months have been surprisingly robust. Thus, it may be premature to lower employment expectations based on just one month's data. The anticipated national employment increases should boost U.S personal income nearly 6% this fiscal year, which is over twice its FY 2003 growth. This is consistent with expected output. The nation's real GDP should grow strongly in FY 2005. Specifically, it is expected to advance 4.5%--its strongest showing during the forecast period.

This *Outlook* summarizes the economic forecast on which the FY 2005 General Fund revenue projections were built. For a complete review of the Idaho Economic Forecast, interested readers are directed to www2.state.id.us/dfm/ief/2004/July/0407ief.html.

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General Fund Update

As of July 31, 2004

	$ Millions		
Revenue Source	FY05 Executive Estimate[3]	DFM Predicted to Date	Actual Accrued to Date
Individual Income tax	968.0	68.9	69.4
Corporate Income tax	118.9	5.4	5.0
Sales Tax	910.8	78.0	82.6
Product Taxes[1]	21.9	1.9	2.1
Miscellaneous	105.7	14.5	14.5
TOTAL GENERAL FUND[2]	**2,125.3**	**168.8**	**173.6**

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of August 2004

General Fund revenue was $4.9 million (2.8%) higher than expected in July, the first month of fiscal year 2005. The gain was due primarily to strong sales tax collections. Slight weakness occurred in the corporate income tax. The new fiscal year 2005 revenue forecast is $7.9 million higher than last January's forecast for 2005. However, several law changes enacted in the 2004 legislative session affect 2005 General Fund revenue and have the effect of shrinking the difference between the two forecasts. Without the law changes the current fiscal year 2005 forecast would be $29.0 million higher than last January's forecast.

Individual income tax revenue was $0.4 million (0.6%) higher than expected in July. On the collection side, filing payments were $0.4 million higher than predicted and withholding collections were $0.3 million higher than predicted. On the payout side, refunds were $1.0 million higher than expected and miscellaneous diversions were $0.7 million lower than expected.

Corporate income tax revenue was $0.4 million (7.1%) lower than expected in July. Filing payments were $0.7 million lower than predicted for the month, while quarterly estimated payments were $0.2 million higher than predicted. Refund payments were $0.1 million lower than expected for the month, while miscellaneous diversions were $0.1 million lower than expected.

Sales tax revenue was $4.7 million (6.0%) higher than expected in July. Sales tax growth is expected to soften in the months ahead as the impacts of rising interest rates are felt in housing and durable goods sales.

Product taxes were $0.1 million (5.3%) higher than expected in July. The strength was primarily in the cigarette tax. Miscellaneous revenue was exactly on target in July.